Exploring Artificial Intelligence's Role in HR to Transform Performance Management using Skills-Based Hiring Strategy

Sree Lekshmi Sreekumaran Nair*
Global Banking School
891 Greenford Road
Greenford
London
UB6 0HE
Email: sreelekshmisreekumar.n@gmail.com
*Corresponding author

Jonathan Liu
University of Wales Trinity Saint David
Winchester House
11 Cranmer Road
London
SW9 6EJ
Email: jonathan.Liu@uwtsd.ac.uk

Ozlem Ozdemir
University of East London
University Way, London, E16 2RD
Email: ozdemirozlem@hotmail.co.uk

Abstract

With the advancement of technology, organisations must consider how such advancements could be adopted to maintain competitive. This paper explores the role of using Artificial Intelligence (AI) in HR to transform performance management using skills-based hiring. Many organisations have used AI in HR to make suitable hiring decisions through human interventions. AI uncovers the skills and competencies needed for the job and makes appropriate decisions on how the hired employee can perform better. This study uses available literature to analyse different studies on AI's role in HR using a skills-based hiring strategy. The study concluded that AI will transform how performance management is monitored, which will help the organisation adapt to the technology. Moreover, through AI, managers can make decisions quickly and provide immediate feedback to the employees. However, the organisation needs to consider the challenges associated with AI. This paper provides a comprehensive overview of various aspects of skills-based hiring and offers practical insights into its long-term adoption for supporting performance management. Theoretical frameworks related to skills-based hiring and examples of real-world challenges HR professionals face are explored.

Track: *Performance Management*

Keywords: *Artificial Intelligence, HR, Performance Management, Skill-Based Hiring Strategy, Systematic Literature Review.*

1. Introduction

Artificial Intelligence (AI) research dates back to the 1950s when Alan Turing published his paper on computing machinery and intelligence, exploring the possibility of machines thinking like humans (Turing, 1950). Over the years, there has been a surge in research on the impact of AI on businesses and how it has revolutionised the business landscape, making it a popular topic for further investigation. AI can support various business functions, including e-commerce, operations, marketing, HR, and after-sales services (Ruiz-Real et al., 2021; Getchell et al., 2022). With the emergence of a hybrid working culture, AI can be leveraged in various ways to achieve desired outcomes. Moreover, AI can be crucial in making informed decisions and enhancing hybrid working environments' potential. AI-driven analytics can monitor and evaluate employee well-being, demonstrating AI's role as a supportive partner in maintaining a healthy work environment. This enables organisations to comprehend the impact of a hybrid working environment on employee well-being, identify areas for enhancement, and provide the necessary support to their employees.

Regarding artificial intelligence (AI) in HR, there are various areas to consider, including recruitment, onboarding, training, performance management, employee engagement, compensation management, employee retention, and career path. However, there is limited evidence on how AI can be utilised in HR activities to support operations using this new technology. AI in HR can automate tasks such as onboarding new employees, training and automating benefits management. Different companies are already using online portals for administrative purposes. This paper focuses on the role of AI in transforming skills-based hiring in HR. Performance management is a crucial aspect of HR that enables employees to receive recognition and constructive feedback while helping management identify high performers and future leaders for retention purposes. However, HR is often busy with day-to-day work, which leaves less time for providing feedback and can result in dissatisfied employees and resignations. AI-driven performance management can help to address this issue by using analytics to improve the relationship between HR and employees, promoting transparency, fairness, and unbiased decision-making. This approach can improve productivity and retention and increase employee satisfaction, benefiting the organisation and leading to a more efficient workforce aligned with the business's strategy. HR should prioritise skills-based hiring over traditional recruitment methods to attract high performers. This discussion paper will explore how AI can help HR transform skills-based hiring during digitalisation and machine learning, providing insights into the potential benefits of AI in HR. This study answers the

research question: How can AI transform performance management using a skills-based hiring strategy? To address this research question, the paper is organised in different sections: Section 2 provides a brief review of the literature in the field of the recent debates on AI on the role of AI in HR activities, skills-based hiring and underpinning theories of skills-based hiring. Section 3 discusses the study's methodology, and section 4 discusses the role of AI in skills-based hiring. Section 5 presents the impact of AI in performance management. Section 6 details the challenges of HR in skills-based hiring. Section 7 presents the conclusion of the study.

2. Literature Review

2.1. The Role of Artificial Intelligence in HR Activities

IBM's research found that 77% of businesses are utilising or exploring the possibilities of Artificial Intelligence. As per Dennison (2023), AI-driven software provides many benefits, such as improved accuracy, efficiency, and productivity in various tasks, enabling businesses to save time and resources. While only 35% of companies currently use AI, 42% are exploring its implementation for future use. Some multinational companies have successfully implemented AI to hire diverse staff, including anonymous resumes and interviewees. Furthermore, the Economist (2018) reported that AI is also being utilised in the healthcare industry, with positive results in oncology. AI is widely used in retail, banking, logistics, travel, education, IT and real estate (Paul et al., 2023). In the retail sector, AI is critical in helping organisations meet customer expectations (Paul et al., 2024). Universities also use AI to screen candidates, conduct admission interviews and select students for university admissions. According to Kanade (2022), Artificial Intelligence (AI) refers to the intelligence of a computer or machine that enables it to replicate human abilities. With various AI technologies, machines can plan, act, and learn like humans. Implementing AI in HR can relieve administrative tasks and paperwork, allowing HR professionals to utilise their time and focus on building relationships with employees and devising strategies. For instance, AI can be employed in HR for talent acquisition, employee learning and development, engagement and retention. HR should identify the questions they need to answer, the issues they want to address, the benefits they seek, and the data required to obtain better results; AI can be an effective tool in this respect.

Heene (1997) conducted research that suggests that the use of competence-based models is an effective tool for human resource management in organisations, particularly when it comes to performance management. However, Liddon (2006) argues that the competence model should focus on employees'

primary abilities, including knowledge, skills, abilities, and behaviours, and the business strategy accordingly to improve employee output. Implementing such strategies can help organisations develop their working models and improve selection, assessment, performance management, training and development, and employee engagement methods, all of which can contribute to better career development. Jain (2017) conducted a study on the use of AI in HR, particularly in functions like recruitment, selection, training, development, and reward management.

The work environment is critical for employees, especially in a hybrid working culture. The Covid-19 pandemic impacted different challenges to the work environment of the people. However, some companies were flexible to offer permanent work from home (Lavelle, 2020). According to Aropah et al. (2020), a comfortable workspace can motivate employees to perform better in their daily tasks. Previous studies (Gajendran & Harrison, 2007; Baltes et al., 1999) also suggest that the work environment positively impacts job performance. Muchtar (2017) suggests that employees can achieve better results with a suitable work environment. Therefore, when evaluating employee performance, it is crucial to consider the work environment factor, particularly during a hybrid working culture (Orissa & Shahrom, 2022).

The hybrid work culture is associated with significant limitations due to the reduced control of supervisors over employees and inadequate support from supervisors, which can negatively affect employee performance and create uncertainties and tension (Van der Lippe & Lippenyi, 2019). Research indicates that team influence can also impact workers as group cohesiveness is positively linked to performance, but lack of interaction can lead to less cohesiveness (Barker, 1993; Sewell, 1998; Cohen & Bailey, 1997). Artificial Intelligence (AI) is considered an appropriate tool to record employee performance and provide historical data for comparison.

Human Resources Management has two main functions: recruitment and selection of employees and their compliance and assessing employee performance and development. Traditional periodic performance management reviews used by HR have several problems, including errors and bias, especially in performance-related pay. The use of AI-enhanced tools for evaluation leads to more accurate and fairer assessments, reducing the time managers require. AI can assess performance more frequently, allowing for predictions of employee performance (Charbonneau & Doberstein, 2020). AI can also integrate with real-time learning modules to help employees improve their performance. AI in HR can enhance decision-

making by professionals by generating more accurate and less biased outcomes, as AI processes data faster and more accurately than humans (Johnson et al., 2022). However, the use of AI in HR is a debatable topic, and companies must consider the ethical implications of its implementation in the workplace. Companies have access to employee data, which they can use in multiple ways, and the ethical performance of employees is influenced by the pressure to perform at work and the organisational and industrial culture rather than independent sources of information (Thiam et al., 2019).

According to several studies (Paul et al., 2024; Duggan et al., 2020; Evans & Kitchin, 2018; Gandini, 2019; Williams & Beck, 2018), using Artificial Intelligence (AI) in the workplace to evaluate employees' performance can provide real-time feedback or comparisons, which can be used as indicators to assess their daily performance and performance goals (Holland et al., 2017; Leicht-Deobald et al., 2019; Woyke, 2018; Zax, 2013). However, it is essential to note that performance evaluation can have a negative impact on motivation (Lepper & Greene, 1975). However, feedback can help employees learn and improve their skills (Vallerand & Reid, 1984). Through AI, employees can receive frequent and effective feedback (Stark & Pais, 2020), which is more updated than traditional performance appraisal systems. However, providing only comparative feedback can hinder the information from the workers (Duggan et al., 2020), which can impact job satisfaction and employee behaviour (Gagne et al., 2021), making employees less autonomous and more competitive.

Implementing machine learning in HR processes has revealed many innovative ways to apply AI in HR functions. Furthermore, various studies have discussed the increasing impact of technology on the HR process, which is growing more rapidly than traditional HR research findings.

2.2. Skills-based hiring

The impact of COVID-19 and increasing inflation rates has potentially led to a rethink of employers' human capital talent management approach (Hancock et al., 2022). During the growth of technology, it is essential to consider skills-based hiring from HR rather than relying on traditional hiring to meet the organisational needs. Often, HR recruits staff with qualifications and experience but lack the appropriate skills suitable for the job. Recruiting staff who lack basic skills for the job is time-consuming and not budget-friendly. To remove this paper ceiling, many big companies such as Boeing, Walmart, and IBM started the programs that gave them importance. IBM began its programs with an emphasis on skills-based

practices. They have removed degree requirements from specific job postings, which demand more skills-based practices to help employees progress from lower to higher-salaried jobs (Hancock et al., 2022). Hiring employees with appropriate skills can increase the number and quality of applications and give internal employees opportunities, leading to excellent retention. It will also create better job opportunities and a diverse employee pool. Through this, employee morale will increase, and their motivation and performance will be boosted as they already have the specific skills for the job.

As per McKinsey's report, Alliance conducted a ten-week Accelerator program to help employers consider skills-based practices when hiring employees (Hancock et al., 2022). The participants were mainly Small and Medium-sized businesses and a few big companies. One of the participants created skills-based job postings; out of 18 qualified applicants, one was hired, and the rest were given other positions within the organisations based on their skills. Also, participants agreed that skills-based job postings increased applications from broader applicants. As per Hunter and Hunter (1984), skills-based hiring is five times more predictive of job performance than hiring for education and more than two times more predictive than hiring for work experience. Santhosh and Lewis (2021) concluded that employees without degrees would stay 34 per cent longer than employees with degrees. As per McKinsey's report, more than 80 per cent of workers who shift to new roles with another employer have the skills to advance in the previous job, but they have not been given internal opportunities to move roles (Hancock et al., 2022).

Skills-based hiring is rising nowadays. First, the reasons for this are the gap in skills for the job roles. As per McKinsey's survey, nearly 9 out of 10 executives agree that their organisations are already experiencing a skills gap or expected within the next five years. It is also challenging for companies to determine applicants' skills from their CVs, and it is difficult to decide whether they are accurate. As with the current technological advancement, HR can adopt AI for skills-based hiring. The second reason is the nature of the current jobs in the changing job market. Many jobs have evolved and are in high demand, so the skills employers were accepting before are changing rapidly. The more demanding skills include interpersonal, cognitive, and systems skills, which have changed from the previous job market demands. It is essential to predict what kinds of new jobs may come into existence shortly (Bakhshi et al., 2017).

For example, AI is now prevailing, and people need to acquire AI skills that are not obtained from traditional qualifications. The third reason is the increase in online learning to develop adequate skills.

Through this, applicants can acquire the skills needed for the jobs through online courses if they cannot achieve a traditional university education. The fourth reason is that there are alternate career paths and self-employment. Millennials, especially, switch jobs more quickly than any other age group. Also, they are more flexible in acquiring new skills (Keeling, 2024). As per Korn Ferry, by 2023, there will be a talent shortage of more than 85 million people (Udemy, 2024). To rectify this, HR needs to reskill and upskill their existing employees and deepen their skill sets. Skill gaps address understanding what skills the employees lack and how to rectify them. The World Economic Forum Future of Jobs Report 2023 discovered that 6 in 10 employees need training before 2027, and they do not have enough resources to make it happen (Udemy, 2024). As per Deloitte, only 5% of executives believe they are investing in the team's upskilling and reskilling to cope with the fast-paced job market (Udemy, 2024).

2.3. Underpinning Theories of Skills-based Hiring

In this paper, we will be focussing on different theories associated with skills-based hiring. The first theory is the Human Capital theory (Schultz, 1960), which has its roots in the early 1960s. As per the theory, human capital consists of the knowledge, skills and abilities of the people employed within an organisation, which results in increased productivity and quality output. The individuals with knowledge, skills and experience are viewed as assets. This theory emphasises investment in education and training, which cause long-term benefits with significant returns. Also, it focuses on the health and well-being of employees, as a healthy workforce is more productive and contributes to the organisation's economy. Individuals acquire skills and knowledge through education and experience; skills-based hiring aligns with this theory by specifying the importance of skills acquired by the candidates.

The second theory is the Resource-Based view (RBV), which states that the organisation's competitive advantage depends on valuable resources and capabilities (Barney, 1991; Penrose, 1959; Peteraf, 1993). This supports skills-based hiring, as the candidate's skill can be considered a valuable resource through which the organisation can achieve its competitiveness. The Competency-Based theory focuses on identifying and developing particular competencies or skills for better job performance at the organisational level. Skills-based hiring aligns with this theory by assessing the applicants' competencies for the role.

When considering cognitive load theory (Sweller, 1988), it is essential to avoid overloading the instructional methods with the capabilities of the individuals. This will hinder the learning process. When applied to hiring, skill-based assessments aim to decrease the cognitive load by concentrating on practical skills and making the evaluation more effective. Also, job matching theory (Jovanovic, 1979) focuses on employees being more satisfied and progressing within their roles when there is a good fit between their skills and job requirements. Through skills-based hiring, the employees will be satisfied and more aligned towards their abilities and the demands of the position. The above theories mainly concentrate on the employees' skills and how they can fit the job role and organisation well.

3. Methodology

The present study uses a literature review and further discusses the role of AI in HR to transform Performance Management using a skills-based hiring strategy. The keywords were used to search databases such as Google Scholar, Web of Sciences, Sage, and ProQuest to carry out the discussions. Since the topic is new, some critical data from the authenticated websites were also considered. The keywords were deployed with different algorithm searches such as ("Artificial Intelligence" OR "AI" OR "Robotics") AND ("Human Resources Management" OR "HRM" OR "HR" OR "HRM functions" OR "Human Resources functions") AND ("Skills-based hiring strategy" OR "Performance Management" OR "employee-level outcome"). Also, only peer-reviewed articles have been included in the literature review. It only focussed on publications in the English language. A thematic analysis was performed to generate themes and codes.

4. Role of AI in skills-based hiring

HR is experiencing a significant challenge to recruit the right person for the right job. With the rapid increase of technology and AI's help, it is more accessible in organisations nowadays. AI can assist HR in planning and making essential recruitment decisions (Karatop et al., 2015). AI can attract and select a talented pool of employees and make decisions faster to handle large volumes of information within a limited time than human capacity (Torres & Mejia, 2017). Using AI algorithms, organisations can improve in identifying candidates more suitable for the job (Budhwar et al., 2022). Also, AI algorithms helped HR identify appropriate candidate profiles, removing biases such as race, gender, and sexual orientation, which would have been impacted if there had been human judgements in the recruitment process.

Using AI in skills-based hiring helps HR in many ways, as human decisions take time. AI can check candidates' backgrounds from public data sources, such as their previous employment and social media profiles. The online Interview Software helps assess facial expressions and speech patterns to assess the candidate's fit within the organisation (Kalia & Mishra, 2023).

Many debates exist on how AI can be used in skills-based hiring, as different organisations still need advancements. In this fast world, HR faces different challenges during recruitment as they need to scan through the CVs, which can also cause bias and missed opportunities. This problem can be rectified through AI as AI can screen CVs and objectively assess applicants' skills and consistency across the process. It is essential to consider the diverse workforce while recruiting. Sometimes, human judgement can be biased unknowingly, affecting the hiring process. AI can eliminate this bias and prioritise the applications only because they have the skills. Through this, the organisation makes sure that skills are valued. HR can also use AI to generate job descriptions and applications. However, the candidates also seek help from AI and use AI to craft their CVs.

Nevertheless, through the new technologies, organisations can accurately assess their skills. AI can also detect undesirable behaviour when the candidates are asked to take assessments such as quizzes and tests. Also, technology can detect whether the actual candidate is taking the tests or whether they are cheating (Koyen, 2023). AI is considered a powerful decision-making tool in which the machine makes the analytics, which HR can analyse and make the choices. For example, AI can identify the strengths and weaknesses of candidates through social profiling and databases. By inputting human judgement into this data, organisations can make the right hiring decisions and predict employee performance for the longer term. Incorporating AI in skills-based hiring allows organisations to become transparent, which is valued by the employees and stakeholders. As the organisation adapts AI into their hiring practice, it is essential to address the ethical concerns.

Organisations must be transparent about algorithmic bias and that hiring is based only on skills. Communication is essential between HR, recruiters and AI developers to balance human decision-making and technological interference (Headworth, 2023). Before skills-based hiring, the organisation can use AI to run an automated skills gap analysis, which helps companies address the areas if they need any help from outside and develop some programmes within the company to address those gaps.

5. Impact of AI in Performance Management

Performance management is a widely discussed topic through which employees receive the recognition they deserve and constructive feedback. This will also help the management find the actual performers and future leaders to focus on their retention. The employees' actual performance depends on their skills for the job role, and if the skills are matched with the job role, then the employee can perform better, and that performance can be measured again using AI analytics. Nowadays, HR is very busy with day-to-day work, which leads to less time to provide constructive feedback and dissatisfied talented employees and their resignations. AI-driven performance management can reduce this situation by using analytics to enhance the relationship between HR and employees. This will also allow the organisation to become transparent, unbiased, and fair to the employees. Through this approach, the organisation can attain improved productivity, better retention, and increased satisfaction of employees. This also positively impacts the business and leads to a more efficient workforce concentrating on the business strategy.

Performance management benefits both employees and the organisation. Employees in the organisation are keen to learn about their performance. However, the organisation is aware of the performance level of the staff and decides who needs the training to improve and increase their performance or update their skills. Also, evaluation is essential to determine who will be penalised, rewarded and promoted depending on employee skills. According to Orlikowski (2000), organisations must use the technological developments that allow them to develop their business to gain a competitive advantage. Through AI, the organisation can improve its performance appraisal systems and encourage employees to provide the correct evaluation system results (Sholihin, 2013). Also, especially with a hybrid working culture, it is essential to track and record the performance of the employees. AI can make this process less time-consuming, and accurate data has been generated.

Artificial intelligence (AI) has become essential to human resources (HR) and has impacted various areas, including recruitment, learning, and employee experience. The next area where AI is expected to make a significant difference is performance management, which relies heavily on data-driven processes that align well with AI and machine learning (ML) technologies. Traditional performance management techniques are often biased, inaccurate, and time-consuming. They rely on subjective evaluations based on recent accomplishments and fail to capture an employee's overall performance potential. On the other hand, AI-powered performance reviews use a vast amount of data and make predictions based on the

current review and the employee's performance and career history. This helps set accurate goals, identify potential promotions, and calculate incentives.

Replacing periodic performance reviews with ongoing reviews has numerous benefits. It allows for continuous feedback and course corrections, making the organisation more agile and flexible. Research suggests that up to 60% of employees prefer continuous feedback. AI-powered systems can continuously collect data from various sources, such as written communication between employees and calendars, providing real-time information on employee performance. This helps managers make quick decisions and provide immediate feedback.

6. Challenges of HR in Skills-based hiring

As per McKinsey's survey before starting the Employer Accelerator program, the participants responded that sourcing, skills validation and increasing skills-based practices are the most common challenges they faced when implementing a skills-based approach. Similarly, the study conducted by McKinsey in 2021 with 300 SMBs revealed that sourcing and validation are considered the top two hiring challenges they have faced, which is displayed in Figure 1.

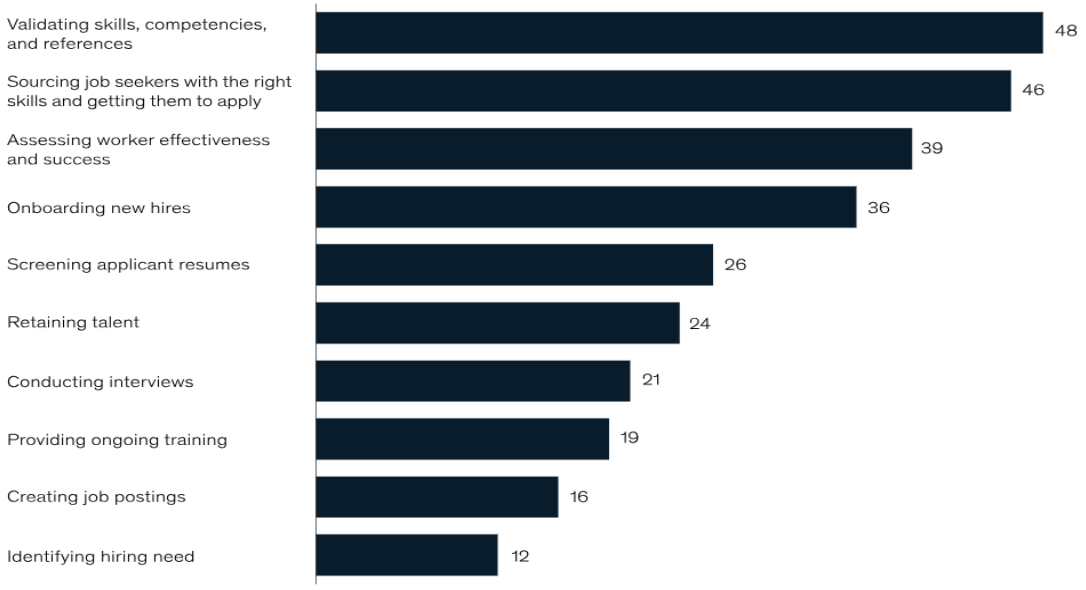

Figure 1: Top hiring and talent challenges, % of respondents indicating step as a top 3 challenge

Source: McKinsey State of Hiring Survey (2021)

The other challenge HR faces is that modern AI platforms must still be functional and fully automated. The most important thing is to use a prompt correctly or describe what AI is supposed to perform. The prompt must be more specific when asking AIs to screen the applicants. HR needs to have critical thinking and problem-solving skills as the output received from AI needs to interpret and analyse the results. When considering the challenges HR faces, they need to clearly understand how to decide which jobs need to produce better candidates and how to communicate the opportunities, especially for lower-wage positions of workers without degrees. HR needs more confidence in discovering better ways to validate employees' skills through interview questions or assessments. HR needs to have a clear understanding of what skills are required for each job role.

Many hiring managers are still resistant to implementing skills-based hiring methods. This is due to the focus towards skills-based hiring and avoiding bias, which makes HR accused of their hiring decision (Keeling, 2024). Some organisations are not up-to-date with the technology, and there are still outdated hiring tools that cannot support skills-based hiring. In some organisations, HR managers use unnecessary job requirements in the advertisement, such as a college degree and years of experience, even if the role is unnecessary. The organisation needs to allocate the resources to upskill and reskill the workforce to increase retention and keep valuable skills in-house for the long-term benefit (Keeling, 2024).

7. Conclusion

In conclusion, AI will transform how performance management is monitored, which will help the organisation adapt to the technology. Also, through AI, managers can make quick decisions and provide immediate feedback to the employees. However, some challenges associated with AI also need to be considered by the organisation and implemented along with skills-based hiring. The resource-based view is considered vital as it is related to organisational competitiveness and is based on the skill set of the employees. This research study has significant implications for both theory and practice. It aims to provide valuable insights into how employers can successfully incorporate AI to hire employees with the necessary skills, enhance performance, and improve management. Additionally, organisations must communicate to their employees the purpose of AI adoption and how it affects performance evaluation. The research also intends to uncover patterns that identify and explain skills-based hiring and how it impacts individual employee performance. This study serves as a foundation for HR Analytics, Head of HR, and HR Directors to recognise the importance of implementing AI in HR. Furthermore, it gives AI developers a

better understanding of the gap between current AI usage and the desired expectations. The study also recommends ways for HR to implement AI for skills-based hiring and performance management actively. As AI is a relatively new area, further research needs to focus on the application of AI in skills-based hiring by HR, where it can screen, validate, and assess job applications by considering the opinions of HR managers/ directors. AI is only applied in larger organisations as they have the budget to implement these resources. It needs to consider the application of AI in skills-based hiring for medium and small and medium businesses. To answer this question, the data requirements for implementing AI in skills-based hiring are essential.

As some of the challenges faced by HR have been mentioned before, it is essential to clearly understand what skills-based hiring means and how AI can be further explored. Future research should focus on the challenges and provide a framework for reducing them, and then HR can confidently recruit based on skills. Future research also needs to consider how HR can rectify job advertisements, mainly by focusing on skills and the challenges faced by this. Future research needs to be conducted with some primary evidence from HR to explore this further.

Also, it is essential to implement AI ethically and morally. Further research can focus on identifying the areas that can contribute to understanding the impact of AI in skills-based training and lead them to practical implementation.

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